

Insights into Informal Cross-Border Trade in Agri-Food Commodities in South Asia

16 May 2024 | Kathmandu, Nepal

EVENT PROCEEDING

South Asia Watch on Trade Economics and Environment (SAWTEE) and the International Food Policy Research Institute (IFPRI) hosted a workshop titled "Insights into Informal Cross-Border Trade in Agri-Food Commodities in South Asia" on 16 May 2024. This collaborative effort aimed to delve into the intricate dynamics of informal trade within the region's agri-food sector.

During the workshop, two presentations were conducted. "Dynamics of Informal Cross-Border Trade," delivered by Ms. Dikshya Singh representing SAWTEE in collaboration with IFPRI, provided valuable insights into the complexities of informal trade dynamics between Nepal and India. Additionally, "A Tale of Two Borders: Informal Agri-Food Trade between India-Bangladesh and India-Nepal," presented by Dr. Mamata Pradhan representing IFPRI and CGIAR India, offered an in-depth analysis of informal trade dynamics between India and Bangladesh. The event was moderated by Dr. Posh Raj Pandey, Chair Emeritus of SAWTEE. The panel discussion featured distinguished participants including Ms. Sabnam Shivakoti, Joint Secretary of the Ministry of Agriculture and Livestock Development; Mr. Anand Bagaria, Managing Director of Nimbus Holdings; and Dr. Ramesh Sharma, Senior Economist formerly associated with FAO, Nepal. Additionally, other participants hailed from various sectors, including former government secretaries, stakeholders in Nepal-India trade, journalists, university professors, organizations representing farmers, and other relevant stakeholders involved in Nepal-China trade.

In his welcome remarks, Dr. Paras Kharel, the Executive Director of the South Asia Watch on Trade Economics and Environment (SAWTEE), emphasized the significant role of informal trade within the broader context of South Asian commerce. Dr. Kharel stressed that informal trade transcends physical borders, extending even to nations with sea borders, such as India and Sri Lanka. Dr. Kharel underscored the importance of quantifying informal trade while acknowledging the need to explore other pertinent factors and issues. These include understanding the nature of informal trade, identifying its driving factors, examining price discovery mechanisms, and elucidating the institutional mechanisms governing such transactions.

Ms. Dikshya Singh's presentation from SAWTEE shed light on the intricate dynamics of informal cross-border trade in selected agricultural commodities between Nepal and India. It revealed that unrecorded imports and exports through Nepal's porous border with India significantly contribute to the country's trade dynamics, challenging the traditional understanding derived solely from recorded figures. The study's qualitative methodology, including desk research, key informant interviews, and focused group discussions, unearthed the various modes and drivers of informal trade, ranging from household imports for consumption to organized informal imports for commercial purposes. Notably, the presentation highlighted the pervasive nature of informal trade in essential commodities such as rice, vegetables, chemical fertilizers, seeds, and even exports like vegetables, paddy, and betel nuts, showcasing its impact on both economies.

Dr. Mamata Pradhan's presentation, titled "A Tale of Two Borders: Informal Agri-Food Trade between India-Bangladesh and India-Nepal," shed light on the intricate dynamics of informal trade in agricultural commodities across these borders. The presentation navigated through the challenges of measuring informal trade and its susceptibility to external shocks, while also exploring its role in economic development. It

provided insights into the institutional mechanisms and transaction costs linked with informal trade, underscoring the necessity for a balanced approach in addressing both formal and informal channels. Additionally, the analysis dissected the specific dynamics and drivers of informal agri-food trade between India and Bangladesh, as well as India and Nepal, revealing the impacts of trade policy uncertainty and regulatory barriers. Concluding with policy implications, the presentation emphasized collaboration, trade facilitation, and infrastructure development to bolster formal trade and bolster local livelihoods.

Dr. Posh Raj Pandey, Chair Emeritus of SAWTEE, highlighted several critical points about cross-border trade. He emphasized that informal trade encompasses legally permitted goods and services that evade regulatory frameworks, such as taxes, certification, and registration requirements, resulting in unrecorded transactions. This is distinct from practices like under-invoicing, under-classification, and non-declaration, which are recorded despite their inaccuracies.

Similarly, Dr. Pandey identified several drivers of informal trade. Firstly, he pointed to disparate agreements between Nepal and India, such as SAFTA, and the complex regulatory requirements and high import and export duties that make the border "thick." Secondly, he noted the non-transparency and divergence of regulations between countries, which increase trade costs and incentivize informal trade to avoid these expenses. Additionally, he mentioned various obstructions and restrictions on product exits, including bans and quotas on certain items. Lastly, domestic policies, such as the substantial agricultural subsidies in India that lower product prices, also contribute to informal trade between India and Nepal.

Mr. Anand Bagaria, Managing Director of Nimbus Holdings, addressed the complexities and implications of informal trade, distinguishing it from illegitimate trade, where the latter involves evasion of taxes. He noted there is no illegitimate and informal trade as such, there is trade where legally produced goods move from one place to another because of financial viability. He noted that historically, people from India would come to Nepal to buy goods like clothing, but this trend has reversed. Mr. Bagaria highlighted several key points: the financial viability and impact of informal trade on government revenue, particularly emphasizing that subsidized fertilizers from India make informal trade lucrative. He stressed the importance of mandatory labeling for all imported products from India, which is often bypassed in informal trade. While acknowledging that informal trade at the household level is difficult to control, he focused on the commercial scale, citing the 1990 border blockade where informal trade played a crucial role in sustaining Nepal. Mr. Bagaria called for clear policy priorities, especially around tariffs, which should be balanced to make tax-evading trade less attractive than formal trade. He highlighted Nepal's dependence on neighboring countries for food security and advocated for corrective measures based on this reality. Emphasizing the importance of quantifying informal trade while implementing corrective measures, he noted that informal trade affects businesses by creating imbalances in revenue, inflation, and risks associated with uncertified products. Mr. Bagaria also pointed out that informal trade is supported by a broader network beyond individual black marketers and suggested that the government could track and regulate these networks if determined. In conclusion, he called for a gradual process to address informal trade, balancing the need for revenue, controlling inflation, and mitigating risks through coherent and strategic policy adjustments.

Dr. Ramesh Sharma, Senior Economist formerly with FAO, Nepal, addressed the complexities of organizing and managing issues related to informal trade. He highlighted the challenge of estimating its size, noting that in the 2009/10 fiscal year, 27 imported and 14 exported commodities were identified. Drawing parallels with Africa, where countries conduct annual surveys on informal trade through central banks or statistical offices, Sharma suggested that Nepal Rastra Bank (NRB) has the resources to undertake similar surveys periodically. He emphasized the importance of focusing on specific commodities rather than the entire sector to understand their market impact and guide policy interventions.

Dr. Sharma proposed several strategies for managing informal trade. First, he advocated for conducting surveys to estimate its size, similar to practices in Africa. Second, he suggested that the Ministry of Agriculture and Livestock Development (MoALD) manage the import market for food products, considering their effect on the market and necessary policy interventions. Third, he recommended that the Ministry of Industry, Commerce, and Supplies (MoICS) address issues related to the Nepal-India Trade Treaty, control of restricted products, and unauthorized trade. Additionally, Sharma proposed compiling and analyzing data on unauthorized trade to understand its implications for livelihoods, food security, and welfare, potentially adopting pre-approved lists of products for informal trade. Finally, he called for reviewing tariffs, para-tariffs, and other barriers to facilitate trade, involving roles for MoICS, NRB, and MoALD.

Dr. Sharma highlighted past mistakes, such as restrictions on sugar, which were based on a poor understanding of the food balance sheet. He suggested that MoALD could lead efforts to identify and tally food balance sheets with informally traded items. He also pointed out discrepancies in mirror data, where some items are not recorded on the exporting side but are reported on the importing side. To address these issues, Sharma advocated for the creation of a pre-approved list of goods up to a certain amount, where authorities would not interfere, drawing on examples from Africa. In conclusion, Dr. Sharma called for coordinated efforts among various ministries to address the issues of informal trade. He emphasized the need for comprehensive data collection and policy interventions that balance the realities of informal trade with the goals of formal economic growth and regulation.

Ms. Sabnam Shivakoti, Joint Secretary at the MoALD, raised critical questions about Nepal's dependency on imports for food security. She emphasized that while government support aims to boost domestic production and export potential, informal trade significantly impacts policy decisions. Restrictions on informal trade often fail to meet demand and production needs, highlighting the necessity of a balanced approach to regulation.

Ms. Shivakoti discussed the implications of tax policies, noting that while the MoALD does not directly control tax regimes, they provide crucial input on how these policies affect agricultural trade. She also underscored the importance of sanitary and phytosanitary (SPS) measures, which, although sometimes viewed as hurdles, are essential for preventing pest invasions and ensuring food safety—citing the example of banana wilt disease entering Nepal due to overlooked inspections. Further, she mentioned that the national single window mechanism has been beneficial in formalizing trade processes, but there needs to be a deeper understanding of its impact on informal trade. Ms. Shivakoti pointed out that informal trade, especially in fertilizers and seeds, often fills gaps left by formal channels, but this sector needs careful management to protect local markets and industries. The discussion included the importance of addressing both the advantages and disadvantages of informal trade, particularly in maintaining food sovereignty and controlling inflation.

Finally, Ms. Shivakoti stressed the need for reviewing and possibly amending policies related to fertilizers and seeds to better support domestic farmers and industries. She highlighted recent amendments in seed registration processes to streamline testing and registration, ensuring quicker access to quality seeds. Overall, her insights call for a comprehensive approach to balancing formal and informal trade, enhancing agricultural productivity, and safeguarding Nepal's food security.

Comments from participants

Mr. Purushottam Ojha, former Secretary of GoN, discussed the informal trade of various commodities such as gold, silver, onions, poppy seeds, edible oil, and black pepper from Nepal to India, noting that tariffs often act as barriers. He highlighted instances of misdeclaration, such as the export of vegetables from eastern Nepal to India where different vegetables were exported under the guise of cabbages. Mr. Ojha proposed two mechanisms: an inter-governmental committee and a customs border office, to address issues in the informal sector. He called for a more comprehensive work plan rather than shallow discussions on these topics.

Mr. Ojha posed a question to Dr. Mamata Pradhan about the role of "*blackia*" (informal porters) who gain employment and social recognition through informal trade. He inquired about potential alternative mechanisms to support these workers. Additionally, he discussed the implications of *border haats* (local cross-border markets) in reducing informal trade, suggesting that such initiatives could play a significant role in formalizing cross-border trade activities.

Mr. Rabi Sainju, former Joint Secretary of the GoN, highlighted several critical issues related to informal trade between Nepal and India. He pointed out the existing policy and coordination gaps within Nepal, emphasizing the importance of addressing food security in cross-border trade. Mr. Sainju attributed the prevalence of informal trade to price differences and the declining agricultural sector in Nepal, noting that the Indian government provides eight kinds of subsidies in the agricultural sector, making Indian products more competitive.

He stressed the need to revise the trade treaty between Nepal and India, particularly addressing the Most Favored Nation (MFN) provision. Sinju also noted that India serves as a distribution hub for South Asia, a potential advantage Nepal has yet to fully exploit. He called for improved coordination between border security forces to better control informal trade and address related issues. Mr. Sainju emphasized that price differentiation and subsidies are significant driving forces behind informal trade and must be addressed in the ongoing trade treaty revisions and trade policy review, which currently focuses more on unauthorized trade with third countries.

Dr. Binod Karmacharya discussed the two-way nature of informal trade between Nepal and India, challenging the common misconception that it primarily flows one way from Nepal. He emphasized the policy implications of the Indo-Nepal Treaty, suggesting a need to revisit and revise the agreement to better control informal trade. Dr. Karmacharya argued that placing the onus solely on Nepal should be reconsidered and that relying on law enforcement agencies might not be a viable solution. Instead, he proposed the formation of a customs union and the liberalization of tariffs through simplified customs procedures. He also highlighted that rules of origin (ROO) pose a hindrance and called for better recording of trade statistics to include both goods and services. Acknowledging the difficulty of completely eliminating informal trade due to the porous border, Dr. Karmacharya suggested that a more practical approach might be to manage and mitigate it rather than attempting full eradication.

Mr. Rajesh Verma, journalist at Clickmandu, commented on the current state of productivity and emphasized the importance of ensuring price viability, particularly concerning dairy products and payments to dairy producers. He pointed out that despite ban on dairy products imports by the Nepal government implemented in February 2024, supply of Indian dairy products have not been affected due to rampant informal imports. Mr. Verma also highlighted the ongoing issue of continued imports from the informal sector and the benefits accruing to informal traders, calling for greater government supervision in this regard.

Dr. Krishna Prasad Panta, senior agriculture economist, underscored the historical connection predating border demarcation and its impact on the informal sector. He advocated for simplifying processes and

enhancing connectivity, noting that trade distortions such as tariffs contribute to the creation of the informal sector. Panta stressed the necessity of formalization to ensure quality control without restricting the informal sector.

Mr. Prahlad Dahal, president, Neppal Dairy Association, raised concerns about lack of oversight at customs borders regarding dairy products, urging for stricter measures to be opted at border crossings if restrictions on formal imports are to yield the desired effect of protecting domestic industries. He pointed out the lack of subsidies and emphasized aligning prices with those in India. Dahal called for proactive solutions and emphasized the importance of addressing underlying problems.

Jaya Poudel, Secretary, Forum for Protection of Consumer Right Nepal, highlighted the need for a study on how informal trade impacts consumer rights and there is no measures to ensure the quality of informally imported agri-food products. They referenced Article 44 of the Constitution of Nepal and advocated for a commercial approach to control informal trade, suggesting the revision of existing laws from a consumer perspective.

Mr. Ishwor Dallakoti, president, Fertilizer Association of Nepal, said that Nepal is highly dependent on informal imports of fertilizers to meet its need, this is especially true for the Terai districts. This happens due to government's inability to supply the fertilizer on time, he pointed out, suggesting to involve private sector in import of fertilizers like India does.

Mr. Panchakaji Maharjan, Chairman, National Farmers Group Federation, pointed out the issues related to imperfect linkages between market and farmers that leads to domestic agricultural products to waste while informally imported products get markets.

Mr. Dipesh Karki, Assistant Professor at Kathmandu University School of Management, discussed the implications of informal food product imports on local farmers and their productivity and suggested assessing impacts of informal imports of services too.

Mr. Laxmi Manandhar, Nepal Hatchery Association, discussed the implications of informal trade on the poultry and hatchery industry, particularly in terms of market competition and the need for policy interventions. He pointed out that Nepali poultry industry, especially hatchery, has been badly affected by informal imports and are finding sustaining difficult. He also called attention to the danger of spread of diseases such as avian influenza due to informal imports of poultry.

Mr. Sudip Bajracharya, from USAID's KISAN II, pointed out that Indian vegetables make their way into Nepali markets easily because they have better supply chain management practices which is lacking in Nepali side. Nepal needs to improve the supply chain and market systems for agri products such as vegetables.

Mr. Krishna Bhakta Shrestha, FNCCI's Agriculture Development Committee Member, highlighted the importance of sustained storage capacity for products and its implications for trade.